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Equities Investment Sciences

SWINGTRADER ULTRA SYSTEM-S2

OPERATIONS GUIDE V1.2

8 MAY 2012

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IMPORTANT NOTICE

ULTRA SYSTEM-S2 is in BETA, meaning it is being tested on live trades with live customers in "out-of-sample" data. As with SYSTEM-S1 BETA performed in early 2011, this process may result in changes to the strategy or techniques mentioned in this guide as part of the improvement process implied by the BETA program. Delivery of S2 for free as part of S1 is temporary. We may elect to charge a separate subscription for S2 at a later stage after BETA testing. S2 is only available to paying S1 customers.

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Introduction

SwingTrader ULTRA System-S2 ("S2") is the 2nd addition to the PowerStocks Research SATOP40 swing trading strategy suite. It joins ULTRA System-S1 ("S1") which was launched in early 2011. The naming of the two systems as S1 and S2 is a tip of the hat to the legendary Richard Dennis, founder of the famous Turtle Traders, which used two trading systems called the same to create millions of dollars profit on the U.S markets with people that had no prior trading experience.

S1 (the old ULTRA+) and S2 are *completely different* in their theory, makeup, strategy, signalling and performance.

The idea is we will have two screens showing on the Join.Me, switching from the one strategy S1 to the other S2.

Why another system?

Any professional trader likes to deploy more than 1 *diversified* strategy in his trading style to reduce "model risk" and capture the widest variety of market conditions. Not every strategy will work well in all markets and quite often after a period of strong gains, a strategy may "lose its mojo" for a while before regaining composure. This is the reason the Turtles traded with two systems. If we have two successful strategies in parallel that are not correlated in any way (i.e. do not use the same mechanics) then we can reduce the risk our results will be affected by this "model risk".

ULTRA (S1) is rather aggressive and quite a big step-up for novice traders of which we are finding we are accumulating many. There is also a requirement among newer, less experienced clients for more sedate strategies with smaller draw-downs, which are psychologically easier to trade, even if their total returns are less. There is a direct link between risk and return in the trading game and unless you are an experienced trader, using aggressive high-risk (but high return) strategies may result in you succumbing to all the psychological risks that result in you sabotaging your own trading results.

The below table is a very high level view of the characteristics of S1 and S2:

SYSTEM CHARACTERISITICS	S1	S2
Trading Risk/Aggressiveness	High	Moderate
Performance in strong market	Excellent	Good
Performance in weak/sideways market	Good	Excellent
Adaptability to broad market conditions	Good	Very Good
Profit taking regime	Moderate	Aggressive
Psychological difficulty/Skill required	Advanced	Moderate
Win Rate on long trades	74%	69%
Gain/Loss ratio on long trades	3.17	4.01
Avg profit on long trades	R8,891	R9,026
Avg loss on long trades	R8,161	R5,086
Win Rate on short trades	58%	78%
Gain/Loss ratio on short trades	2.7	3.9
Average profit on Short trades	R16,839	R5,010
Average loss on short trades	R8,992	R4,782
Win rate all trades	67%	74%
Highest Loss	R17,740	R11,558
Gain/Loss all trades	2.85	3.97
Number of trades in 3 years	84	77
Total return over last 3 years	894%	589%

Clearly S1 is higher risk but higher return than S2.

But beginners are likely to get better gains from S2 than S1 due to less errors being made from a skills/psychological perspective.

If we are coming out of a huge correction and you suspect a strong rebound, then S1 will clearly be the better strategy.

If we are in the late stages of a bull market and the market is "tiring" then S2 will be the better strategy.

If you are unsure as to the future condition of the market, then S2 may be the safer play.

What are the differences between S1 & S2?

First, we need to be clear that S2 is NOTHING LIKE S1 apart from the visual interface on Join.Me you have come to know and love.

So there will be a standard equity curve at the top, followed by a positions indicator below it, followed by the TOP40 Index chart with signals and a trailing stop, followed by an Overbought/Oversold indicator pane and then followed by a proprietary momentum indicator used for the generation of BUY and PROFIT TAKING signals. Finally at the bottom of the page we have a standard point accumulator showing how many points we have made and locked-away on the trade.

S2 has a robust profit-taking strategy during the course of a trade to minimise losses. This is why her maximum drawdowns are so small. However S2 does not have profit targets we can display on the chart like S1. Certain momentum objectives have to be met to trigger profit taking actions and it is indeterminable at what index price points these actions will take place. We can see where the momentum indicator has to get to generate a profit taking signal and how far it is to get there, but we can't translate that into a specific profit objective on index price.

S1 blue line acts as trailing stop and major technical support whereas S2 uses a 2-week Donchian lower channel as trailing stop of last resort which is more short-term support. Thus risk is VARIABLE with the S2 stop whereas it was FIXED per trade with S1. This requires manual calculations for proper position sizing for each trade. However, tables have been created for beginners that closely approximate trade risk.

Many S1 users will have realised by now that profit targets and the blue line are very strong indicators of major support and resistance levels. In fact many clients use these to trade INTRADAY i.e. trade the swings between support and resistance on a daily basis in parallel to the standard ULTRA trade. There is none of this with S2. S2 will not be as intraday friendly as S1

S2 is very much simpler to S1. There are 5 contracts on the longs and 5 on the shorts. There are no class-A, B, C trades to worry about

S2 has longer long trades and shorter short trades than S1.

As S2 is more sedate than S1 it works more consistently across a broad set of market conditions. ULTRA S1 can experience periods of sideways to negative equity curve whereas S2 chugs steadily upwards with very brief periods of negative to sideways equity curves.

If we have a strong bull market, S1 will out-perform S2. Ditto strong bear market. But in a sideways to slightly down market, S2 outperforms S1. Over 3 years S2 achieved only 80% of the performance of S1 but it was a much smoother ride getting there.

The performance of S1 and S2 since March 2009 (when this Bull market started) with R50, 000 starting capital are shown overleaf as at 30 April 2012, with major differences highlighted. They both traded with 5 IG-Markets SATOP40 micro-contracts of R600 margin each and 100:1 gearing.

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Detailed report: (S2)

Statistics | Orders list | Trades list

	All trades	Long trades	Short trades
Profit & Loss (net total)	294,734.03	182,684.03	112,050.00
Total profit	394,034.41	243,725.41	150,309.00
Total loss	-99,300.38	-61,041.38	-38,259.00
Total profit / Total loss	3.97	3.99	3.93
Number of trades	77	39	38
Percentage of winning trades	74.03%	69.23%	78.95%
Winning trades	57	27	30
Losing trades	20	12	8
Even trades	0	0	0
Trade expectancy (Total P&L / Nbr tr...	3,827.71	4,684.21	2,948.68
Average profit on winning trades	6,912.88	9,026.87	5,010.30
Average loss on losing trades	-4,965.02	-5,086.78	-4,782.38
Standard deviation on profit and loss	6,555.58	8,003.62	4,451.17
Highest profit	19,510.00	19,510.00	9,110.00
Highest loss	-11,558.00	-11,558.00	-7,552.00
Avg time in the market (nbr of bars)	10.19	16.67	3.55
Avg time beetween trades (nbr of ba...	1.82	3.63	3.73
Avg time on winning trades (nbr of b...	11.67	21.15	3.13
Avg time on losing trades (nbr of bars)	6.00	6.58	5.12
Avg time on even trades (nbr of bars)	n/a	n/a	n/a
Percent of time in the market	85.06%	85.06%	85.06%
Total brokerage fee	9,192.00	4,152.00	5,040.00
Highest nbr of consecutive winning t...	7	6	6
Highest nbr of consecutive losing tra...	3	2	3
Drawdown (highest loss of the equit...	26,690.16	25,091.00	32,856.03
Highest gain of the equity curve	297,594.94	163,858.00	47,904.38
Return on initial capital (Profit&Loss/I...	589.47%	365.37%	224.10%

Detailed report: SwingTraderULTRA (S1)

Statistics | Orders list | Trades list

	All trades	Long trades	Short trades
Profit & Loss (net total)	447,216.25	194,738.25	252,478.00
Total profit	688,666.44	284,512.44	404,154.00
Total loss	-241,450.19	-89,774.19	-151,676.00
Total profit / Total loss	2.85	3.17	2.66
Number of trades	84	43	41
Percentage of winning trades	66.67%	74.42%	58.54%
Winning trades	56	32	24
Losing trades	28	11	17
Even trades	0	0	0
Trade expectancy (Total P&L / Nbr tr...	5,324.00	4,528.80	6,158.00
Average profit on winning trades	12,297.62	8,891.01	16,839.75
Average loss on losing trades	-8,623.22	-8,161.29	-8,922.12
Standard deviation on profit and loss	11,816.87	8,437.61	14,493.57
Highest profit	31,446.00	15,870.00	31,446.00
Highest loss	-17,740.00	-16,180.00	-17,740.00
Avg time in the market (nbr of bars)	9.95	13.79	5.93
Avg time beetween trades (nbr of ba...	1.05	2.07	2.17
Avg time on winning trades (nbr of b...	11.41	14.56	7.21
Avg time on losing trades (nbr of bars)	7.04	11.55	4.12
Avg time on even trades (nbr of bars)	n/a	n/a	n/a
Percent of time in the market	90.58%	90.58%	90.58%
Total brokerage fee	14,940.00	5,100.00	9,840.00
Highest nbr of consecutive winning t...	11	11	9
Highest nbr of consecutive losing tra...	5	2	5
Drawdown (highest loss of the equit...	94,200.00	80,226.00	102,068.02
Highest gain of the equity curve	539,183.00	146,119.09	295,861.31
Return on initial capital (Profit&Loss/I...	894.43%	389.48%	504.96%

You can see that S2 traded 77 times versus S1 84 times but more importantly that S2 is in long winning trades for 21 days on average versus S1's 14 days. S2 catches nice longs trends in the spirit of "let your winners run". S1 is prone to cutting out prematurely on long trends due to meeting all her profit objectives. Another important observation is that S2 maximum losses for longs and shorts are FAR LOWER than the old S1 especially on the shorts. This is much more sedate. Another observation is the stunning 78% success rate on the S2 shorts but S2 holds shorts for an average 3 days taking whatever profit shows itself off the table very quickly and getting out. It is "sniping" at its best. Finally the win rate on the longs for S1 is 74% and S2 is only 69% but you will note the gain/loss ratio for the longs for S2 is 3.99, superior to ULTRA S1's 3.17. This is because S2 cuts losers short and lets her winners run and there are very wide profit targets.

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The best way to visualise these statistics is the 3-year equity curves since March 2009 as shown below. S1 has suffered as a result of the shorts more recently not going her way, sapping whatever profits she is eking out on the longs due to massive volatility. Should this market return to a strong bull or bear she will pick up her skirts again. Note we have advised clients to stay clear of the S1 shorts for about 4 months now. Without the short trades, S1 has done far better than that shown below.
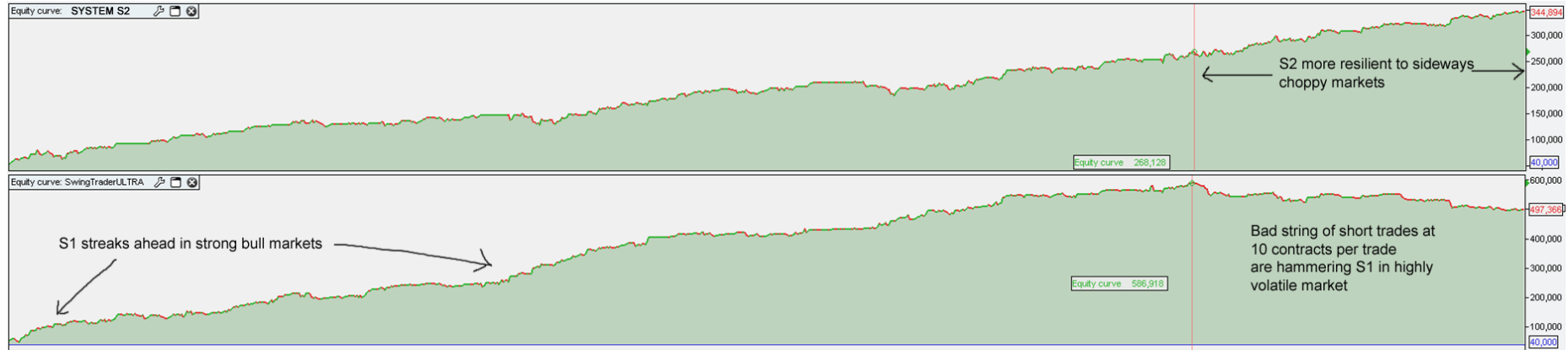
Look how S1 streaked ahead of S2 at the start of this bull market and after the end of each major stock market correction, while S2 is a sedate "slow and steady" upward curve. Since Sept 2011 (vertical red line) the shorts have hammered S1 (longs have been ok) but S2 maintained her slow and steady climb.

Multiple System Usage Guidelines

If you are a beginner, than regardless of which system you trade, stick to long-trades only. Beginners should favour S2 over S1 for their long trades as the aggressive profit taking regime will result in continued profits been banked and boosting confidence.

If you have a higher risk appetite and requisite advanced skills, then deploy S1. However, if you are an intermediate to advanced trader, and assuming you have at least R100, 000 trading account, then we recommend deploying BOTH STRATEGIES IN TANDEM. This means running both systems concurrently.

If we are coming out of a major +10% corrections or a massive bear market then go overweight S1. If you suspect the market is tiring and losing momentum then go overweight S2.

Want to try the best of both? Then play S1 longs and S2 shorts as 1 single strategy, call it S3. We will be testing this as a separate system soon!

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Live Signal Chart Usage Guidelines
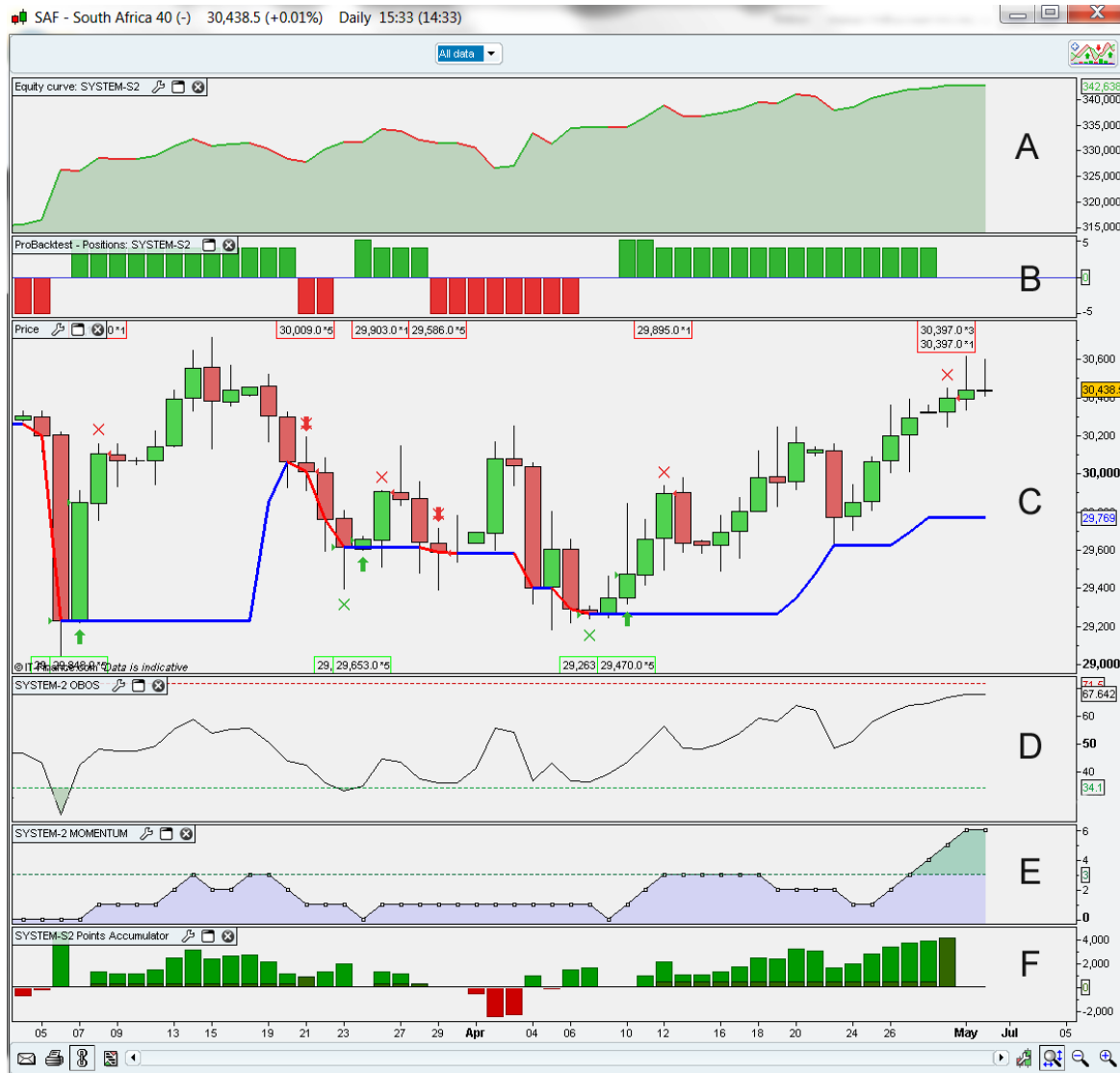
The S2 Live Signal is broadcast on the Internet for subscribers, similar to that shown on the left.

PANEL-A shows the equity curve or the size of the trading account that started with R50, 000 in March 2009. As ULTRA S2 makes profits it moves up in real time and vice versa.

PANEL-B is the positions indicator and shows how many positions long (green) or short (red) we are.

PANEL-C shows the SATOP40 index (daily bars, but the right-most bar updating in real time.) It also shows:
1. Green up-arrows (Buy signals),
2. Red crosses (sell contracts to bank profit),
3. Red down arrows (short the market)
4. Green crosses (cover/close your shorts.)

Finally it has the dark blue line that acts as trailing stop of last resort. When the SATOP40 index closes below the blue line we sell all long contracts we are holding and short the market.

PANEL-D is the Overbought/Oversold indicator. When it rises up through 34.1 from below then it is a BUY 5 CONTRACTS signal. When it falls from above to below 71.5 it is a SELL 1 CONTRACT signal.

PANEL-E is our proprietary momentum indicator. When it rises from 0 to 1 it is a BUY 5 CONTRACTS signal. When it rises from 3 to 4 it is a SELL 3 CONTRACTS signal. When it rises from 4 to 5 it is a SELL 1 CONTRACT signal.

PANEL-F is the point accumulator showing us how much profit (in points) we are in the trade and how much of this is BANKED due to profit-taking actions. (Dark green section.)

End of day system

ULTRA S2 is an end-of day system. This means it makes its trading decisions at the end of the trading day, or when the candle for the day closes, at about 12AM in the morning.

To follow the system perfectly you would need to be awake at this time to execute the trade, but more often than not, after 9PM at night, the US market closes and no other markets are open and very little happens. You could safely make a trade decision after 9PM that is not likely to change until the candle closes unless of course the decision point is sitting right on a particular threshold. For the most part, decisions can be made on convincing moves though where it will be quite safe to assume the condition that triggered a particular action will not change.

As for S1 we recommend clients take profits the minute the requisite profit taking targets are met and not wait for the end-of-day signal confirmation.

Shortly after this guide was published, we launched ULTRA S2/RT which is a "real-time" version of S2 that takes profits intraday on profit target strikes. You are strongly urged to continue your learning about S2 and consult the ULTRA S2/RT Addendum Guide after completing this document, in order to properly operate the live system we are broadcasting for clients.

Tradable Instruments

ULTRA has been optimised for and operates in a live environment with the SharenetCFD's IG Markets SA TOP40 Index-CFD that mathematically tracks the SA TOP40 (J203) index and trades 24x5. You can execute trades against this Index-CFD via 3 contract variations that all provide a 150x gearing on your initial margin:

1. R400 margin micro-contract at R2 per index point
2. R2,000 margin mini-contract at R10 per index point
3. R10,000 margin contract at R50 per index point

There are 9 things we like about this Index-CFD.

1. It is liquid as it trades globally. Liquidity is very important.
2. Secondly, it trades 24x5. This is useful to capitalise on out-of normal hours swings and suits the times of those that trade in the evenings after their normal day jobs. You also have the safety of getting out before the market opens locally if a major geopolitical event were to occur.
3. Third, the gearing at 150x means you can start out a trading regime with relatively little funds.
4. Fourth, you can hold the contract as long as you like without worrying with SAFEX futures expiration and roll-overs and the like.
5. Fifth, the 3 contract sizes cater for all pockets.
6. Sixth, it's only 10points brokerage and is very cheap to trade.
7. Seventh, you can trade fractions of contracts, very important for small accounts.
8. Finally, it pays dividends on the underlying shares. This last point was an unexpected bonus when alpha-testing ULTRA on live money trades and we were taken aback at how this can boost returns.
9. IG markets have really neat apps for Android and Apple Smartphones and Tablets from which you can view your account and make trades on-the-go after receiving SMS's from us.

Note that all back-tests/performance figures we refer to in this document, EXCLUDED dividends pay-outs from any performance comparisons. We also excluded daily interest costs payable on the loan portion of the derivative instruments and interest received on un-deployed cash portions of the trade account. As we experienced with ULTRA S1, interest is not expected to make significant degradation to quoted performance figures.

Buy (Long) Signals

The following conditions triggers BUY 5 CONTRACTS (long) signals, assuming you're not already long:

1. OBOS moves from below 34.1 to above 34.1 [CLASS-A LONG]
2. MOMENTUM moves from 0 to 1 [CLASS-B LONG]

Both Class-A and Class-B longs are equally good. Under certain circumstances however, they are stronger (better) than most occasions and have higher confidence levels.

The lower the OBOS signal troughed and the longer the MOMENTUM was sitting on 0 before it rose to 1, the better the signal!

Sell (Take profit) Signals

ULTRA S2 has an aggressive profit-taking regime to lock in profits. This has the effect of boosting your psychology and lowering loss rates. It is said in trading circles that knowing when to sell is more important to knowing when to buy and this is especially true with the two ULTRA products.

When you are in a long trade, your profit taking rules are as follows:

1. SELL 1 CONTRACT when the trade has made 0.84% or more gains
2. SELL 3 CONTRACTS when MOMENTUM rises from 3 to 4
3. SELL 1 CONTRACT when MOMENTUM rises from 4 to 5
4. SELL 1 CONTRACT when OBOS falls below 71.4 (could occur multiple times)

Unlike S1, there are no specific profit targets on the SATOP40 index except for the first rule. For the 1st rule, you can program an automatic sell order on 0.84% above the system entry price. The other rules cannot be translated into specific SATOP40 index price targets in advance. This is one reason some traders prefer S1 to S2 as this means you are going to have to be available to execute the trade when it occurs.

Shorting Signals

S2 only shorts under the following two rules:

1. CLASS-A: When OBOS falls below 74.1 from above and *no more long contracts are in hand.* Profit objective target is around 2.5%-2.8% from trade entry depending on volatility. 10 of these since Mar '09, 80% win rate, 4.9-to-1 gain/loss ratio

2. CLASS-B: SATOP40 Index falls below the blue trailing stop (stop changes from blue to red.) Profit objective target = around 1%-1.2% from trade entry depending on volatility. 29 of these since Mar '09, 72% win rate, 3.4-to-1 gain/loss ratio.

When rule 2 triggers, you <u>CLOSE ALL LONGS at the same time you go short</u>. Rule 2 is your stop of last resort. You know this up-front in the trade and so can put it in as an automatic sell.

Covering Shorts

The process of closing your short trade is called "covering" your shorts. You have to buy back all the contracts you took out on loan to short. The rules for this are very simple:

1. BUY 5 CONTRACTS when the underlying index falls
    a. CLASS-A : 2.5%-2.8% or more from entry price
    b. CLASS-B : 1%-1.2% or more from entry price

2. ABANDON THE SHORT when losses on trade exceed 3% on the underlying entry price

There is no profit-taking regime for the shorts. You get in and you get out. When you have made your profit objective on the trade you take it all off the table and sit in cash for the next long. You have to be nimble.

Rule 2 ensures we cap our maximum loss if we really made a bad call. It has never been triggered in its 3 year history but you never know. We have to cap a potential wild loss somehow to allow proper position sizing and risk management.

The nice thing with the short covering rules is that you can equate them back to a specific SATOP40 index price the moment S2 makes the trade. This means you know upfront what your target is (just like S1) and you can thus put in automatic BUY orders to close the trade in your absence.

Profit Objective Markers (POM's)

As we stated in the beginning, S2 does not have profit objectives linked to the underlying SATOP40 index values as with S1 except the first long profit target and the short profit targets.

We have therefore decided to show POM's for these on the Live Trading Chart on the Internet, as ULTRA subscribers like using POMs to pre-program their exits into the dealing system so a profit taking action can be triggered in their absence.

LONG POM
When S2 enters a long, a POM will be presented on the trading chart which is "around" 0.85% from trade entry depending on volatility.

There are no other POM's for the long trades, as the 2nd, 3rd and 4th targets are objectives that must be met by OBOS and MOMENTUM.

The 1st profit target is not there to make money; it is there to take profits off the table to reduce the risk of the whole trade turning into a loss by a *considerable margin*. Of the 39 long trades since Mar '09, all but 5 (87%) reached 1st profit target.

SHORT POM's

S2 uses SATOP40 index-price profit objectives just like S1, but there are *two classes of shorts:*

1. *CLASS-A Short*, when OBOS falls below 71.5 from above and no long trades are in hand
   Objective target = around 2.5%-2.8% from trade entry depending on volatility.
   10 of these since Mar '09, 80% win rate, 4.9-to-1 gain/loss ratio

2. *Class-B Short*, when SATOP40 falls below the blue line (support)
   Objective target = around 1%-1.2% from trade entry depending on volatility.
   29 of these since Mar '09. 72% win rate, 3.4-to-1 gain/loss ratio

It stands to reason Class-A shorts are better opportunities than Class-B shorts but they are much more rare events.

Sample use of 1st LONG and SHORT POM's as described in the graphic below:

Optimal Contract Sizes

ULTRA-S2 always trades in batches of 5 contracts. This initial figure is tied specifically to optimal performance under the various profit taking rules.

We know for best historic performance, it is wise to sell 1/5th or 20% of your positions on the 1st long profit target. Likewise, we know it best to dispose of 3/5th or 60% of your original holdings (3/4 or 75% of your current holdings) when MOMENTUM rises from 3 to 4.

Whatever amount of contracts you open a trade with, make sure it is easily divisible by 5. Remember there are 5 micros to each mini and 5 minis to each standard contract.

You can buy 5 micro, mini or standard contracts. It is always easiest to just buy 5 micro-contracts instead of 1 mini-contract. They are identical margin and exposure but taking profit with the 5 individual micro contracts is going to be easier than selling fractions of your mini contract.

If your account is too small to buy 5 micro-contracts, then you can buy 1 micro contract and sell off fractions of it. IG allows you to do this. So for instance if you go on a long with 1 micro contract, you can dispose of 0.2 contracts on your first profit target being met, leaving you with 0.8 contracts. Similarly, when MOMENTUM rises from 3 to 4 you then sell 0.6 contracts, leaving you with 0.2 contracts.

Optimal Risk Management

Just like ULTRA, you need disciplined position sizing and risk management for S2 trades. This means you must ensure you do not trade too large.

This is the NUMBER ONE reason for traders failing – they trade TOO BIG and with no thought to risk or the worst case loss.

Your first survival rule for ULTRA S2 is to ensure you never risk more than 2.5% of your account on any one trade. Without exception! As profits & your experience grow, you can move this to 5%

Looking at the above rule this means if you start with R50, 000, then you do not want to be risking more than R1, 250 per trade. If the trade goes horribly wrong, you do not want to lose more than this amount.

The first thing you notice with this rule is that as you start winning and your account starts growing, you can trade larger and larger amounts. But if you hit a losing streak and your account size starts dropping, the rule will scale your trade sizes back accordingly. Go large when you are winning, pull back when you are losing.

It is mathematically impossible to wipe out your trading account if you follow this risk-management rule.

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Optimal Position Sizing

With our risk management capping our losses to 2.5% of our account, we now turn our attention to how many contracts we can trade. This is called *position sizing*. We need to consider all the things that could result in us incurring the maximum budgeted 2.5% loss (the R1, 250 in the prior example.)

Unlike ULTRA-S1, we do not have our worst case losses mathematically computed up-front by the dynamic blue trailing stop. This means we are going to have to figure out another way to calculate appropriate position sizing for long trades.

We could consider the following historical facts about ULTRA long trades:

1. Maximum loss encountered in 3 years was R11,558 with opening trades of 5 micro-contracts
2. Average loss encountered in 3 years was R5,086 with opening trades of 5 micro-contracts

S2 LONG 2.5%	Conservative	Optimisitic
R 25 000	0.3	0.6
R 50 000	0.5	1.2
R 75 000	0.8	1.8
R 100 000	1.1	2.5
R 125 000	1.4	3.1
R 150 000	1.6	3.7
R 175 000	1.9	4.3
R 200 000	2.2	4.9
R 225 000	2.4	5.5
R 250 000	2.7	6.2

If we wanted to budget for the *worst loss* experienced in the past then we can calculate that we can only trade R1, 250/R11, 558*5 = 0.11*5 = 0.54 micro contract with a R50, 000 account. This is the uber-conservative approach recommended for beginners.

If we wanted to budget for the *average loss* experienced in the past then we can calculate that we can only trade R1, 250/R5, 086*5 = 0.24*5 = 1.23 contracts.

This is the more optimistic approach to position sizing for every R50, 000 in your trading account, recommended once you trade account has accumulated some profits and you have at least 3 wins under the belt.

The proper amount of micro-contracts you can trade for various account sizes is shown in the above table for both the conservative and the more optimistic trading styles using the 2.5% risk management rule.

There is one more option available to calculate position sizing. It is probably the best, but requires a bit of calculation BY YOU. As opposed to "conservative" and "optimistic", we call this "dynamic". It uses the BLUE trailing stop of last resort. Since this line caps your loss because of Shorting Signal Rule #2 it is IDEALLY SUITED for position sizing.

Dynamic Stops [Harder work, but far superior method]

With ULTRA S1, the blue line always mathematically capped your maximum loss to 3% of the underlying no matter what our entry point. The S2 stop, which is a 2-week lower Donchian support level, is a dynamic moving target and will always be a varied distance from your entry point. This is why you have to calculate distance-to-stop manually and why the numbers of contracts you can trade will VARY FROM TRADE TO TRADE.

The Donchian stop is the most superior method of computing position sizing and will result in far higher returns and lower losses than the back-tested model that just trades a fixed amount of 5 contracts. But extra effort will be required by you to:

1. Calculate the distance from your entry point to the blue stop line (R)
2. Using R, & your money left M, calculate how many contracts you can trade (C)
3. Manually calculate how many contracts to sell on each profit take

Look at the long-trade setup on 10 April 2012 below (upward green arrow) where the ULTRA S2 system had R334, 432 in her account and played 5 contracts @ 29,470. S2 was being reasonable here as our rules in the previous section allows for 3.6 to 8.2 contracts, premised on a repeat of an average and historic worst case loss respectively. But this conservatism is costing her dearly;
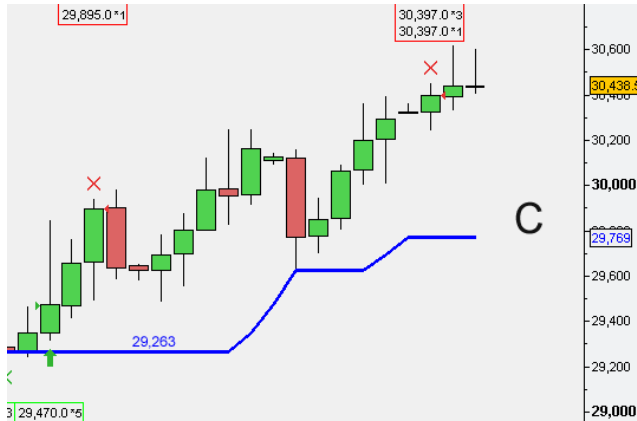
At the time of entering this trade we were quite close to the blue stop and you would have seen on the right hand side of the Live Signal screen that the blue line was reading 29,263. So you could have computed upfront that your maximum points risk R=29,470-29,263 = 207 points. You would add another 20 points for brokerage (10 point spread on the buy & sell respectively) plus 100 points for slippage giving you 327 points of risk if the trade went belly up before hitting any profit targets.

Now you know the micro-contracts are R2.00 per point so your risk R equates to R2x327=R654 per micro contract. Assuming you have R50,000 left in your account, you risk management rule dictates we lose no more than R1,250 per trade meaning you can trade R1,250/R654=1.9 contracts versus the 0.5 to 1.2 of the rules in the previous section.

But hold on, ULTRA had R334, 000 in her account, so her risk budget could have been 2.5% of that or R8, 350. She could easily have traded R8, 350/R654=12.76 contracts! So in this example, ULTRA made far less profit than she could have.

But now look at another example when we open a trade MUCH FARTHER from support as shown on the left.

Here, R= 29,848-29,228=620 points. Add 120 points for brokerage & slippage for a 2x740=R1, 480 risk per micro-contract. That's almost 2 times as much risk as the previous example!

In this case ULTRA should only have purchased R8, 350/1,480 = 5.6 contracts. In this example, she traded the correct amount!

Manually calculating how many contracts you can trade is the far superior position sizing method but you can probably get away with using the standard contract table for a hassle free trading experience. For small accounts you will want to use the manual method to maximise the amount of contracts you can trade, since the tables will sometimes suggest less than is actually possible.

Tactics with "small" trading accounts

We are cognisant of the fact that many clients have "small trading accounts" whereby the risk management and position sizing rules limit you to less than 1 micro-contract on a trade. There are a few techniques for dealing with sub-1 fractional micro contracts as described below.

FIRST APPROACH – DYNAMIC STOP MANUAL CALCULATION

This is *first prize*, but *may not yield a solution*. You have to do the calculation to see if you can use it. This approach is discussed at bottom of page 13 "Dynamic Stops [Harder work, but far superior method]". Essentially you look at the distance between where you want to enter and the S2 blue line (support) to define your "risk" and calculate how many contracts you can trade. Under certain circumstances, even with small accounts, *when the index is close enough to the blue line* the position sizing calculation MAY ALLOW YOU MORE THAN 1 CONTRACT. Under these circumstances the tables may show less than one allowable contract but the calculation shows you 2 sometimes even 3!

SECOND APPROACH - TRADESENSE

This is the consolation prize. For 6 weeks after opening a new account, IG gives you "TradeSense" which is the ability to purchase sub-1 fractional contracts. In this case if the position sizing table on Page 13 tells you that you can only purchase 0.4 contracts, then that is exactly what you do!
Just enter "0.4" into the SIZE field of the trading ticket and you are done!

S2 LONG 2.5%	Conservative	Optimisitic
R 25 000	0.3	0.6
R 50 000	0.5	1.2
R 75 000	0.8	1.8
R 100 000	1.1	2.5
R 125 000	1.4	3.1
R 150 000	1.6	3.7
R 175 000	1.9	4.3
R 200 000	2.2	4.9
R 225 000	2.4	5.5
R 250 000	2.7	6.2

THIRD APPROACH – GO OPTIMISTIC

This increases your risk, but still to a level that is not deemed "overboard". It more than doubles your allowable contracts *but this does not double your risk*. Essentially it means using the 2nd column "Optimistic" in the position sizing guideline table. The assumptions made in "Conservative" & "Optimistic" are based on how we calculate how much we can <u>expect</u> to lose if the trade goes sour. In "Conservative" we assume we are going to incur *the worst case historical* loss. This is probably *a bit too overboard*, but that is why it's called "Conservative". In "Optimistic" we are being realistic and whilst acknowledging we *could* incur the worst case loss we are betting we are only *likely* to incur the "average" loss.

FOURTH APPROACH – "RATCHET BACK"

In this approach, you buy 1 micro contract. Now you are OVEREXPOSED and need to deal with it. There are 3 ways to deal with it:

ONE: Ditch the remaining contracts immediately. The transaction cost with IG is not onerous and this is a perfectly valid strategy. It costs a bit more, but not as much as the trade going wrong with an oversized position! If your allowance is 0.6 contracts, you buy 1 and immediately afterwards sell 0.4 contracts. You are now "right sized". It costs about R50 for the "ditching" exercise per micro contract.

TWO: If after buying the single contract you see the trade going your way, let 100 or 200 points accumulate in your favour before "rightsizing". This more than makes up for your transaction costs. If however the trade is going against you after opening the single contract, *immediately ditch* the extra weight you are carrying.

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THREE: Shoot for the *training wheels target*. In this instance you chase the 1st profit target shown by S2/RT, the "training wheels" shown by small dots. You will need to read the S2/RT (Real-time) Addendum Guide to understand what we are talking about here.

When this is hit you offload the extra baggage. We know this target is hit 85% of the time so by chasing this target with the "oversized" portion of your contracts, you are essentially reducing your risk.

The "training wheels" target is *much lower* than the official 1st profit target so it stands to reason that statistically it is MORE LIKELY TO BE STRUCK. After hitting the training wheels target, you are now "right-sized" and let the balance of the trade run to full term on the strategy 1st profit target (the large dots on the S2/RT chart.)

PLEASE DO NOT SIMPLY GO IN WITH 1 CONTRACT if it means double what you are allowed. Time and time again we see losses attributed to over-betting. It is the SINGLE MOST PREVALANT factor in outsized losses. Not only are your losses outsized if the trade goes sour, but the raised risk has raised the stakes considerably and AMPLIFIED your emotional quotient in the trade. When this happens you are FAR MORE LIKELY to sabotage your trade due to greed or fear, especially when markets are volatile.

Shortly after this guide was published, we launched ULTRA S2/RT which is a "real-time" version of S2 that takes profits intraday on profit target strikes. You are strongly urged to continue your learning about S2 and consult the ULTRA S2/RT Addendum Guide in order to properly operate the live system we are broadcasting for clients.

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Detailed Trade Statistics

Detailed report: SYSTEM-S2 — 4 Mar 2009 to 2 May 2012

Statistics | Orders list | Trades list

	All trades	Long trades	Short trades
Profit & Loss (net total)	292,637.84	186,274.84	106,363.00
Total profit	394,756.22	247,316.22	147,440.00
Total loss	-102,118.38	-61,041.38	-41,077.00
Total profit / Total loss	3.87	4.05	3.59
Number of trades	77	39	38
Percentage of winning trades	72.73%	69.23%	76.32%
Winning trades	56	27	29
Losing trades	21	12	9
Even trades	0	0	0
Trade expectancy (Total P&L / Nbr tr...	3,800.49	4,776.28	2,799.03
Average profit on winning trades	7,049.22	9,159.86	5,084.14
Average loss on losing trades	-4,862.78	-5,086.78	-4,564.11
Standard deviation on profit and loss	6,618.15	8,024.15	4,548.73
Highest profit	19,510.00	19,510.00	9,110.00
Highest loss	-11,558.00	-11,558.00	-7,552.00
Avg time in the market (nbr of bars)	10.30	16.79	3.63
Avg time beetween trades (nbr of ba...	1.79	3.58	3.68
Avg time on winning trades (nbr of b...	12.00	21.33	3.31
Avg time on losing trades (nbr of bars)	5.76	6.58	4.67
Avg time on even trades (nbr of bars)	n/a	n/a	n/a
Percent of time in the market	85.36%	85.36%	85.36%
Total brokerage fee	9,240.00	4,140.00	5,100.00
Highest nbr of consecutive winning t...	7	6	6
Highest nbr of consecutive losing tra...	3	2	3
Drawdown (highest loss of the equit...	26,690.16	26,436.82	39,866.20
Highest gain of the equity curve	294,522.78	163,894.81	46,677.98
Return on initial capital (Profit&Loss/l...	585.28%	372.55%	212.73%

Detailed report: SYSTEM-S2 — LAST 30 TRADES

Statistics | Orders list | **Trades list**

⬆ Entry date	Exit date	Type	Bars Nbr	Abs Perf	Relat Perf	Brokerage fee
10 Apr 2012	30 Apr 2012	Long	17	8146.0	2.763605	120.0
29 Mar 2012	08 Apr 2012	Short	8	3110.0	1.0625601	120.0
25 Mar 2012	29 Mar 2012	Long	4	-156.0	-0.05259514	120.0
21 Mar 2012	23 Mar 2012	Short	2	3840.0	1.2964606	120.0
07 Mar 2012	21 Mar 2012	Long	12	1680.0	0.5627394	120.0
16 Feb 2012	06 Mar 2012	Short	16	9110.0	3.116238	120.0
23 Dec 2011	16 Feb 2012	Long	43	13830.0	4.816127	120.0
13 Dec 2011	14 Dec 2011	Short	1	4780.0	1.7003417	120.0
22 Nov 2011	13 Dec 2011	Long	18	7662.0	2.7546287	120.0
18 Nov 2011	21 Nov 2011	Short	2	8940.0	3.2468915	120.0
03 Oct 2011	18 Nov 2011	Long	40	19510.0	7.4730873	120.0
28 Sep 2011	30 Sep 2011	Short	2	6630.0	2.5467634	120.0
09 Aug 2011	28 Sep 2011	Long	43	8102.0	3.1344771	120.0
26 Jul 2011	27 Jul 2011	Short	1	4640.0	1.6618967	120.0
14 Jul 2011	26 Jul 2011	Long	10	-4240.0	-1.4718115	120.0
06 Jul 2011	11 Jul 2011	Short	4	4030.0	1.4144778	120.0
21 Jun 2011	06 Jul 2011	Long	13	10420.0	3.776598	120.0
15 Jun 2011	17 Jun 2011	Short	2	3140.0	1.1531353	120.0
13 Jun 2011	15 Jun 2011	Long	2	-2840.0	-1.0205567	120.0
08 Jun 2011	10 Jun 2011	Short	2	3660.0	1.3191104	120.0
24 May 2011	08 Jun 2011	Long	13	6214.0	2.188027	60.0
23 May 2011	24 May 2011	Short	1	-3500.0	-1.231873	180.0
06 May 2011	23 May 2011	Long	14	-2718.0	-0.95388293	120.0
04 May 2011	05 May 2011	Short	1	3510.0	1.247561	120.0
19 Apr 2011	04 May 2011	Long	12	6152.0	2.14715	120.0
13 Apr 2011	18 Apr 2011	Short	4	7890.0	2.8047323	120.0
17 Mar 2011	13 Apr 2011	Long	23	14600.1875	5.2749395	120.0
10 Mar 2011	15 Mar 2011	Short	4	6169.0	2.2571206	120.0
25 Feb 2011	10 Mar 2011	Long	11	-6671.0	-2.312851	120.0
22 Feb 2011	23 Feb 2011	Short	1	4714.0	1.645112	120.0
31 Jan 2011	21 Feb 2011	Long	18	12584.406	4.456508	60.0
28 Jan 2011	31 Jan 2011	Short	2	2725.0	0.9645939	180.0

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Trade & Signal Catalogue 04 Mar '09 to 25 Aug '09

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Trade & Signal Catalogue 25 Aug '09 to 05 Feb '10

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Trade & Signal Catalogue 07 Feb '10 to 25 Jun '10

Trade & Signal Catalogue 25 Jun '10 to 10 Nov '10

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Trade & Signal Catalogue 10 Nov '10 to 24 Mar '11

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Trade & Signal Catalogue 24 Mar '11 to 11 Aug '11

Trade & Signal Catalogue 11 Aug '11 to 23 Dec '11

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Trade & Signal Catalogue 23 Dec '11 to 2 May 2012